A. The Scope of the Public Interest Inquiry

While the public interest inquiry generally may provide the Commission with "broad discretion . . . to consider factors relevant to the achievement of the goals and objectives of" the legislation, Michigan Order ¶ 385, it is limited by Congress's specific determinations.[26] In the 1996 Act, Congress decided that it would open local markets by enacting a competitive checklist that sets forth concrete obligations in plain terms. The "checklist" was Congress's test of "what . . . competition would encompass," 141 Cong. Rec. S7972, S8009 (daily ed. June 8, 1995) (statement of Sen. Hollings), and Congress forbade the Commission from second-guessing its judgment or modifying its checklist "by rule or otherwise." 47 U.S.C. § 271(d)(4) (emphasis added); see also 141 Cong. Rec. S8188, S8195 (daily ed. June 12, 1995) (statement of Sen. Pressler) (noting adoption of checklist approach in place of "actual competition" test). As the Chairman of the Senate Commerce Committee reassured Senators, "[t]he FCC's public-interest review is constrained by the statute" because "the FCC is specifically prohibited from limiting or extending the terms used in the competitive checklist." 141 Cong. Rec. S7942, S7967 (daily ed. June 8, 1995) (statement of Sen. Pressler). Accordingly, the Commission may not use the public interest inquiry to add local competition criteria beyond those that Congress included in the checklist.

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[26] See NAACP v. FPC, 425 U.S. 662, 669 (1976) ("the use of the words 'public interest' in a regulatory statute . . . take meaning from the purposes of the regulatory legislation"); New York Central Sec. Corp. v. United States, 287 U.S. 12, 25 (1932) ("the term public interest' as thus used [in a statute] is not a concept without ascertainable criteria"); Business Roundtable v. SEC, 905 F.2d 406, 413 (D.C. Cir. 1990) ("broad 'public interest' mandates must be limited to 'the purposes Congress had in mind when it enacted [the] legislation'") (quoting NAACP v. FPC, 425 U.S. at 670).

The Michigan Order nevertheless suggests that public interest approval should be conditioned in every case on exceeding the checklist. The Commission reasoned that because Congress (1) wanted the Bell companies to enter long distance only after local markets are open and (2) included both the competitive checklist and the public interest test in section 271, Congress must have viewed the competitive checklist as an inadequate mechanism to open local markets.[27] But in fact, Congress wanted the Commission to examine an essential element of Bell company interLATA entry not addressed by any other part of section 271: the competitive consequences of that entry, given the checklist and section 272's safeguards.[28] The Commission's equation of the public interest inquiry with its own assessment of local competition is implausible on its face, for it assumes that Congress devoted countless hours to honing the smallest details of the checklist and forbade the Commission from altering them, see 47 U.S.C. § 271(d)(4), and yet wanted the Commission to use a different standard of open local markets as the dispositive test in considering BOC applications.[29]

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27. See Michigan Order ¶ 389 (reasoning that if "compliance with the checklist alone is sufficient to open a BOC's local telecommunications markets to competition," then "BOC entry into the in-region interLATA services market would always be consistent with the public interest requirement whenever a BOC has implemented the competitive checklist") .

28. See Michigan Order ¶ 388 (discussing "congressional determination" that open local markets and regulatory safeguards will protect interLATA competition); see also 141 Cong. Rec. S7972, S8012 (daily ed. June 8, 1995) (statement of Sen. Hollings) ("we have had every particular safeguard that you can imagine, that the lawyers could think of . . . to make sure that it works and works properly for the public interest").

29. See, e.g., 141 Cong. Rec. S8188, S8195 (daily ed. June 12, 1995) (statement of Sen. Pressler) (describing extensive negotiations and work that went into developing the competitive checklist).

The point of the public interest test is thus to allow the Commission to examine the effect on competition of Bell company entry into the interLATA market. Accordingly, the principal focus of the inquiry must be the market where the effects of Bell company entry would directly be felt: the interLATA market. It cannot be the local market, for issues related solely to local competition are conclusively determined by compliance with the competitive checklist.

The Commission may as part of its public interest inquiry evaluate such matters as the current state of long distance competition and the degree to which the checklist, section 272, and other regulatory safeguards constrain anticompetitive conduct in the interLATA market. These inquiries are familiar for the Commission. As long as a decade ago, for example, the Commission addressed the hotly contested issue whether regulatory safeguards and market conditions were then sufficient to preclude the Bell companies from impeding competition in long distance. The Commission concluded that they were and thus agreed with the Department of Justice that the MFJ's line of business restrictions should be lifted, notwithstanding that the Bell companies in 1987 had no obligations to competitors comparable to the checklist.[30]

The Commission also may consider individual circumstances that Congress could not have anticipated — such as the applicant's history of compliance or non-compliance with Commission rules. See Michigan Order ¶ 397. The Commission may not, however, use the public interest inquiry to substitute its own local competition plan for that established by

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30. Responsive Comments of the Federal Communications Commission As Amicus Curiae on the Report and Recommendations of the United States Concerning the Line of Business Restrictions Imposed on the Bell Companies by the Modification of Final Judgment, at 58, United States v. Western Electric Co., No. 82-0192 (D.D.C. filed Apr. 27, 1987).

Congress. Over-regulation of local and long distance markets today cannot be defended in the name of ideal competition tomorrow.[31] The Commission also may not use the public interest inquiry to rewrite express provisions of the Act.[32] In particular, the public interest test may not be used as a vehicle for circumventing the specific statutory restrictions of sections 251 and 252 regarding such matters as the pricing of UNEs and resold services. Although this issue is now pending before the Eighth Circuit,[33] that Court just recently confirmed that this Commission does not have "jurisdiction over intrastate telecommunications matters" under the Communications Act unless Congress has drafted provisions that "expressly apply to intrastate telecommunications matters and explicitly direct the FCC to implement the act's intrastate

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31. MCI Telecommunications Corp. v. FCC, 627 F.2d 322, 341 (D.C. Cir. 1980) ("The best must not become the enemy of the good."); see generally 47 U.S.C. § 271(d)(4); Conference Report at 1 (enacting a "de-regulatory national policy framework"); 141 Cong. Rec. S7895 (daily ed. June 7, 1995) (statement of Sen. Hollings) ("We should not attempt to micro-manage the marketplace"); 141 Cong. Rec. H8282 (daily ed. Aug. 2, 1995) (statement of Rep. Bliley) (Congress wanted to promote "competition, and not Government micro-management of markets"); accord Local Interconnection Order, 11 FCC Rcd at 15509, ¶ 12 ("look[ing] to the market, not to regulation" to determine entry strategies); see also Hausman Aff. ¶ 10 ("The Commission is once again failing to recognize that regulation is meant to benefit consumers, not to further other objectives of regulators.").

32. See NAACP v. FPC, 425 U.S. at 669; United Sav. Ass'n v. Timbers of Inwood Forest Assocs., Ltd., 484 U.S. 365, 371 (1988) (when "only one of the permissible meanings produces a substantive effect that is compatible with the rest of the law" statutory provision's meaning is "clarified by the remainder of the statutory scheme") (internal quotation marks omitted); National Broadcasting Co. v. United States, 319 U.S. 190, 216 (1943) (the public interest "is to be interpreted by its context").

33. See Petition of the State Commission Parties and the National Association of Regulatory Utility Commissioners for Issuance and Enforcement of the Mandate (filed Sept. 17, 1997) & Petition for Immediate Issuance and Enforcement of the Mandate (filed Sept. 18, 1997), Iowa Utils. Bd. v. FCC, No. 96-3321 (8th Cir.).

requirements."[34] Because section 252 reserves pricing authority to the States, and the public interest provisions of section 271 do not purport to override that delegation of authority, the FCC is powerless to usurp State jurisdiction over pricing through the section 271 process.

B. The Current Long Distance Oligopoly Limits Competition

The Commission has long held that the benefits of new entry in long distance presumptively outweigh any risk of harm,[35] even where the long distance entrant is an incumbent local exchange carrier.[36] That presumption is especially apt when applied to this application.

The interexchange market is highly concentrated and systematically non-competitive. The Department of Justice, for example, has concluded that competition in the long distance business is "decidedly imperfect" and there is "room for more competition."[37] Legislators who

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34. California v. FCC, 1997 U.S. App. LEXIS 22343, at *10 (emphasis in original) (citing Louisiana Pub. Serv. Comm'n v. FCC, 473 U.S. 355, 376-77 (1986)).

35. See Report and Order, Inquiry into Policies to be Followed in the Authorization of Common Carrier Facilities to Provide Telecommunications Serv. off of the Island of Puerto Rico, 2 FCC Rcd 6600, 6604, ¶ 30 (1987) ("plac[ing] a burden on any entity opposing entry by a new carrier into interstate, interexchange markets to demonstrate by clear and convincing evidence that [additional] competition would not benefit the public") (emphasis added); Report and Third Supplemental Notice of Inquiry and Proposed Rulemaking, MTS-WATS Market Structure Inquiry, 81 FCC 2d 177, 201-02, ¶ 103 (1980) (Commission will "refrain from requiring new entrants to demonstrate beneficial effects of competition in the absence of a showing that competition will produce detrimental effects").

36. See Inquiry into Policies To Be Followed in the Authorization of Common Carrier Facilities to Provide Telecommunications Serv. Off of the Island of Puerto Rico, 2 FCC Rcd at 6604, ¶ 30 (Commission's "open entry policy," "clearly contemplate[s] competitive entry by independent local exchange companies") (citing MTS-WATS Market Structure Inquiry, 81 F.C.C. 2d at 186).

37. Memorandum of the United States in Response to the Motion of the Bell Companies' Motion for Generic Wireless Waiver at 22, United States v. Western Elec. Co., No. 82-0192 (D.D.C. filed July 25, 1994); The Antitrust Reform Act: Hearings on H.R. 3626 Before the Subcomm. on Economic and Commercial Law of the House Comm. on the Judiciary, 103d Cong., 2d Sess.

crafted the 1996 Act agreed that the long distance industry is "oligopolistic." 141 Cong. Rec. S7881, S7889 (daily ed. June 7, 1995) (statement of Sen. Pressler). Although it has found that AT&T no longer retains unilateral market power, the Commission also has acknowledged that AT&T, MCI, and Sprint may jointly be engaged in non-competitive, cooperative pricing. Order, Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, 11 FCC Rcd 3271, 3313-15, ¶¶ 80-84 (1995). In the Michigan Order, the Commission repeated its "concern[s] that not all segments of this market appear to be subject to vigorous competition," and "about the relative lack of competition among carriers to serve low volume long distance customers." Michigan Order ¶ 16.

In a competitive market, entry by new firms and competition by incumbent firms drives prices toward cost. See Schmalensee Aff ¶ 9 (App. A at Tab 11); Paul W. MacAvoy, The Failure of Antitrust and Regulation to Establish Competition in Long-Distance Telephone Services 173-74 (1996) ("MacAvoy Study"). Yet long distance carriers have failed to pass on cost savings to their customers. AT&T, MCI and Sprint have benefitted from the Commission's reductions in access charges, which constitute nearly half of interexchange carriers' total costs. Hausman Aff. ¶ 30. From January 1990 to July 1996 access charges declined by 27 percent, yielding at least a 13 percent reduction in interexchange carriers' total costs during that period. Id. Yet carriers have raised their prices despite these declines in access charges. See Schmalensee Aff. ¶ 9 (9% drop in access charges between 1993 and 1996, while AT&T raises rates 22%); Hausman ¶¶ 28-32. Indeed, they have raised prices despite additional savings, over and above access charge

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(1994) (statement of Assistant Attorney General Anne K. Bingaman).

declines, due to new transmission technologies and lower equipment prices. Id.; see Schmalensee Aff. ¶ 9; MacAvoy Study at 96; WEFA Study at p. 11 (App. C at Tab 62) (failure to pass through cost reductions of 6 to 7 percent per year).

In addition, the major carriers have raised their discounted rates along with the basic rates off of which discounts are taken. Hausman Aff. ¶ 31; see Schmalensee Aff. ¶¶ 11, 16-17 (discounted rates yield "supracompetitive profits"). Recent flat-rate promotions, moreover, do not mark a substantial departure from the longstanding pattern of lock-step price increases. Schmalensee Aff. ¶¶ 12-14; Hausman Aff. ¶ 32. AT&T's flat rate of 15 cents per minute — higher than its standard evening rate — does not benefit typical residential callers who place most calls during off-peak hours. Schmalensee Aff. ¶ 13. MCI's flat rate of 14.5 cents and Sprint's two-tiered plan of a 25 cent peak rate and 10 cent off-peak rate also provide at most modest relief.[38] The monthly consumer price index for interstate toll calls rose steadily during 1995 and 1996, with only minor declines in early 1997. See WEFA Study at p. 10. As Professor Schmalensee points out, "the only reason that many consumers find the One Rate plan attractive today is that AT&T has substantially raised its basic rates over the last several years." Schmalensee Aff. ¶ 14.

To the extent that there have been price reductions, they consist simply of passing only a portion of the interchange carriers' savings from recent access charge reductions, and were effected only because the Commission required AT&T to share some of its windfall with residential consumers who pay undiscounted basic rates. See Hausman Aff. ¶ 32 (noting that

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[38]. See AT&T Calls MCI Flat Pricing More Than a Coincidence, Newsbytes, Sept. 30, 1996.

none of the access charge savings was passed on to discount customers). In a competitive industry, regulators do not need to strong-arm competitors into passing on cost-savings to consumers. See Schmalensee Aff. ¶ 9.

The major carriers themselves concede that they do not compete for the business of the lowest volume callers. See id. ¶ 15. They have in the past claimed that these customers are served below cost, but that does not explain why mid-volume callers are denied discounts. See id. ¶¶ 15-17. Besides, even if claims of below-cost pricing were true, they would only highlight the need for additional facilities-based competition to place pressure upon all carriers to lower operational and marketing costs.

C. Market Evidence Confirms that BellSouth's Entry into the InterLATA Market in South Carolina Will Benefit Consumers

BellSouth's entry into interLATA services in South Carolina will provide the needed competition and benefit long distance consumers through lower prices and/or higher quality service. Moreover, by chipping away at costly barriers between local and long distance services, BellSouth's entry will bring further benefits. The United States is the only nation in the World that divides local from long distance telephone service and thereby deprives consumers the benefits of both integration and of additional formidable competitors in long distance. Hausman ¶¶ 26-27; see also Gilbert Aff. ¶ 44 (App. A at Tab 3). Despite hypothetical possibilities of anticompetitive conduct, every other country that has permitted competition in long distance has decided that the benefits of allowing incumbent LECs to participate outweighs possible anticompetitive concerns. Hausman Aff. ¶ 26. The record of incumbent LECs' competitively beneficial provision of vertically related services makes clear that the unanimous conclusion of all these other nations is correct.[39]

1. Evidence of Competition Where LECs Have Been Allowed to Offer Long Distance.

Uniform historical experience confirms the potential benefits of in-region interLATA entry by BellSouth. As the Commission itself has recognized, the "recent successes of [SNET] and GTE in attracting customers for their long distance services illustrates the ability of local carrier to attract a significant share of the long distance market rapidly;" "recent studies" based upon these positive market experiences "have predicted that AT&T's share of the long distance market may fall to 30 percent with BOC entry;" and that such "additional competition in the long distance market is precisely what the 1996 Act contemplates and is welcomed." Michigan Order ¶ 15.

Long distance customers in Connecticut have benefitted from SNET's price competition since it entered the interstate market in 1994.[40] On average, SNET's residential long distance rates have been 17-18 percent lower than AT&T's. Hausman Aff. ¶¶ 16-19. These savings have especially benefitted low-volume callers who, prior to SNET's entrance, had disproportionately

39. In addition to the evidence regarding U.S. markets discussed below, evidence from these foreign markets confirms that American consumers are suffering from extension of the MFJ prohibition. In Canada, where carriers use essentially the same equipment as in the United States to serve less densely populated areas, long distance rates are actually lower than in this country. Hausman Aff. ¶ 26; see Gilbert Aff. ¶ 44 & n.70. And in the United Kingdom, competition has developed to the vertically integrated incumbent notwithstanding that local markets are significantly less open than in the United States. Gilbert Aff. ¶ 44.

40. Consumers of intrastate services also have benefitted, as AT&T responded to SNET's long distance offerings with competitive intrastate offerings. See Gilbert Aff. ¶¶ 37-38.

stayed with AT&T because they were ignored by other carriers. See Schmalensee Aff. ¶¶ 25-28. SNET has shown both a willingness and ability to compete for this segment of the market: whereas its share of revenues is 20 percent, its share of customers is half-again as high.[41]

In order better to compete with SNET, AT&T petitioned the Commission for authority to reduce its long distance rates specifically in Connecticut.[42] AT&T's stated reason for the petition was "the rapidly emerging competition from SNET in Connecticut."[43] AT&T thus effectively admitted that it faces more intense competition in Connecticut than elsewhere because the incumbent LEC has been allowed to enter the long distance market.[44]

The two geographic corridors running from New York City and Philadelphia to New Jersey offer another example in which incumbent local exchange carriers — in this case Bell Atlantic and NYNEX — have competed in in-region, interLATA services by setting prices below those of the major carriers. AT&T concedes that Bell Atlantic's corridor rates are as much as one-third lower than AT&T's,[45] and credits Bell Atlantic's widespread marketing of "sav[ings]

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41. See Susan Jackson, A Telecom Yankee Defends its Turf, Business Week, Oct. 28, 1996, at 167.

42. See AT&T Comments, Market Definition, Separations, Rate Averaging and Rate Integration, at 29, Policy and Rules Concerning the Interstate, Interexchange Marketplace & Implementation of Section 254(g), CC Docket No. 96-61 (FCC Apr. 19, 1996) ("AT&T Rate Averaging Comments"); AT&T Corp.'s Petition for Reconsideration, Policy and Rules Concerning the Interstate, Interexchange Marketplace at 2-5 (FCC Sept. 16, 1996); see also supra at 3-4 (discussing nationwide rate increases).

43. AT&T Petition for Reconsideration at 2.

44. See id. at 2-5; AT&T Rate Averaging Comments at 29.

45. AT&T Corp.'s Petition for Waiver and Request for Expedited Consideration, AT&T Petition for Waiver of Section 64.1701 of the Commission's Rules, CC Docket No. 96-26 Attachment A

over AT&T's basic rates" for Bell Atlantic's 20 percent market share of interstate corridor calls.[46] See Taylor Aff. at p. 18 (App. C at Tab 62). AT&T and MCI sought permission to reduce their rates in these corridors precisely because they face more intense competition there than elsewhere.[47] Neither questions that consumers in these corridors are better off because of price competition from the incumbent Bell company.[48]

2. *BellSouth Is Suited to Break Up the Interexchange Oligopoly in South Carolina*

BellSouth will offer consumers these same sorts of competitive benefits when it provides in-region, interLATA service in South Carolina.

BellSouth has an affirmative incentive to lower long distance prices in South Carolina, because increased interLATA usage will increase usage of BellSouth's access services as well. See Hausman Aff. ¶¶ 12-14. Indeed, the SCPSC noted that BellSouth already had prepared a proposed intrastate, interLATA tariff with initial basic rates that are "at least 5% lower than the corresponding rates of the largest interexchange carrier." Compliance Order at 6; see App. D at Tab 8 (proposed tariff).

(FCC filed Oct. 23, 1996) ("AT&T Waiver Petition").

46. Id. at 3.

47. See id. at 1, 5; MCI Comments at 1, AT&T Petition for Waiver of Section 64.1701 of the Commission's Rules, CC Docket No. 96-26 (FCC filed Nov. 18, 1996) ("MCI Comments") (petitioning the Commission "so that [MCI] likewise will be in a position to benefit consumers by being able to compete effectively against Bell Atlantic and AT&T").

48. See AT&T Waiver Petition at 5 (consumers in the corridors, unlike other areas, "benefit from the highest degree of competition possible"); MCI Comments at 3 ("fully support[ing]" AT&T's "arguments").

BellSouth is, moreover, well-positioned to spur the competition that will lower interexchange prices. BellSouth has honed its marketing skills as a wireless carrier in South Carolina, as well as a provider of other competitive offerings such as exchange access to business customers, Centrex service, customer premises equipment, and directories. These experiences will enable BellSouth to provide better interexchange services to South Carolinians and to sell them effectively. See Schmalensee Aff. ¶¶ 30-37. BellSouth also could reduce costs by using existing sales and customer support systems (in compliance with the requirements of section 272). See Gilbert Aff. ¶¶ 24-28; Schmalensee Aff. ¶ 29. Indeed, AT&T secured approval to acquire McCaw in part on these grounds. Applications of Craig O. McCaw, 9 FCC Rcd 5836, 5885, ¶ 83 (1994), aff'd sub nom. SBC Communications Inc. v. FCC 56 F.3d 1484 (D.C. Cir. 1995).

Above all, however, BellSouth's brand name will make it a strong competitor to the three major incumbents. The BellSouth brand is recognized by approximately 70 percent of consumers in region — less than AT&T and MCI, but high in relation to other potential entrants into long distance. Gilbert Aff. ¶ 17. BellSouth's reputation is on par with that of the major incumbent interexchange carriers: better than three out of four customers rated BellSouth as "very good" in the categories of customer service and service reliability/product quality. Schmalensee Aff. ¶ 32. These factors will give BellSouth lower marketing costs in-region than other potential new entrants and position BellSouth as a serious competitor to AT&T, MCI, and Sprint.[49]

BellSouth's marketing strength will be most pronounced among current BellSouth customers who are part of a low-volume market segment that is "neglected in the competition among interexchange carriers." Schmalensee Aff. ¶ 26. The failure of the three large carriers to market services to this group leads many residential and small business customers to choose AT&T out of inertia, without giving other carriers serious consideration. Indeed, the evidence demonstrates that most current competitors to the major interexchange carriers focus on high-revenue customers, not on residential users or small businesses. Id. ¶¶ 27-28. If BellSouth (and other Bell companies across the country) can make competitive inroads, however, AT&T, MCI, and Sprint are likely to respond with new promotions and expanded eligibility for targeted offerings, to the benefit of low-volume callers. Id. ¶ 37.

Likewise, BellSouth will be able to offer bundled service offerings and "one stop shopping." See Compliance Order at 6-7. Bundled service packages can "have clear advantages for the public," such as greater convenience and the ability to secure volume discounts by aggregating purchases of different services.[50] The Commission thus has supported developments

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49. See Schmalensee Aff. ¶ 37; Gilbert Aff. ¶ 28; see also Applications of Craig O. McCaw, 9 FCC Rcd at 5871-72, ¶ 57 (finding that AT&T acquisition of McCaw would serve public interest due to AT&T's brand name, financial strength, marketing experience, and technological know-how).

50. Applications of Craig O. McCaw, 9 FCC Rcd at 5878-80, ¶¶ 73-75; see 141 Cong. Rec. S713 (daily ed. Feb. 1, 1996) (statements of Sen. Harkin) (1996 Act will allow "low cost integrated service with the convenience of having only one vendor and one bill to deal with"); S. Rep. No. 104-23, at 43 (1995) (joint offerings constitute a "significant competitive marketing tool"); see

that promise to speed the introduction of bundled services at the retail level. This was one reason why the Commission approved AT&T's buyout of McCaw Cellular Communications, saying it "would deny users the current and prospective benefits of bundling only if presented with a compelling public interest justification" for doing so. 9 FCC Rcd at 5880; see Gilbert Aff. ¶ 19.

BellSouth will not be the only, or even the first, carrier to market bundled offerings, and will have no unfair advantage in providing bundled packages. See Gilbert Aff. ¶¶ 7-16. Indeed, the SCPSC found that BellSouth's "entry into the interLATA market will give [its] customers the same opportunity as customers of other South Carolina telephone companies (i.e., GTE in Myrtle Beach and Sumter; Sprint-United in Beaufort and Greenwood; Rock Hill Telephone Co. in Rock Hill and York) to choose one provider for all their telecommunications needs." Compliance Order at 6-7.

Moreover, bundled offerings are the cornerstone of interexchange carriers' plans for entering the local exchange. AT&T, for example, has announced that it plans to "take a basic $25-a-month long distance customer and convert him or her into a $100-a-month customer for a broader bundle of services." AT&T Challenges the Bell Companies," Wall St. J., June 12, 1996, at A3; see Gilbert Aff. ¶¶ 7-19 (describing AT&T's plans). MCI is offering long distance, cellular service, Internet access, and MCImetro local service on the same bill in some States. Gilbert Aff. ¶ 10. Sprint is bundling its long distance offerings with local wireline service, cable television, and PCS offerings. Id. ¶¶ 11-14. Following MFS Communications' merger with the

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also Gilbert Aff. ¶ 16 ("Consumers will benefit from the integration of service offerings and the marketing of bundled products through convenience and through the increased number and variety of telecommunications options available in the marketplace."); Hausman Aff. ¶ 7.

with the Internet access provider UUNet and the long distance carrier WorldCom, the merged entity's President explained: "We are creating the first company since the breakup of AT&T to bundle together local and long distance service carried over an international end-to-end fiber network owned or controlled by a single company." Communications Firms to Join in $12 Billion Deal, Los Angeles Times, August 27, 1996, at A-1 (see also Gilbert Aff. ¶ 15).

A recent study by J.D. Power and Associates found that 65 percent of households are likely to sign up with one company for all their telecommunications services, with the majority choosing their current long distance carrier as that sole provider. Gilbert Aff. ¶ 18. Congress recognized the importance of bundled offerings to the development of local and long distance competition, noting that a "full 86 percent of . . . small business owners want one-stop shopping for telecommunications services" and that "[t]wo-thirds of them want to be able to choose one provider that can give them both local and long-distance telephone service." 141 Cong. Rec. S7903 (daily ed. June 7, 1995) (statement of Sen. Burns). Legislators in fact considered bundling so important that they barred the major interexchange carriers from jointly marketing resold local service with their own long distance services until the incumbent Bell company has an equal ability to combine local and long distance offerings. 47 U.S.C. § 271(e)(1).

Approval of BellSouth's petition also will lift remaining prohibitions on BellSouth's participation in telecommunications equipment manufacturing and allow BellSouth to pursue all opportunities in this area, subject to statutory and regulatory safeguards. See id. § 273(a); S. Rep. No. 104-23, at 67 (allowing Bell Companies to engage in manufacturing will "foste[r] competition . . . and creat[e] jobs along the way"). Finally, approval of this application would trigger "1+" intraLATA competition in South Carolina, intensifying competition in the intraLATA toll market as well. See Compliance Order at 6; 47 U.S.C. § 271(e)(2). BellSouth is submitting along with this application a detailed implementation plan for intraLATA dialing parity. Varner Aff. ¶¶ 199-201 & Ex. AJV-8. The rivalry between SNET and AT&T and Connecticut — which quickly spilled over from interstate services to intrastate toll — indicates how, in a world of bundled service offerings, greater competition in interLATA services will benefit South Carolinians across a range of telecommunications services including local and intraLATA toll. See Gilbert Aff. ¶¶ 34-38; Hausman Aff. ¶¶ 10 n.13, 22.

While it is difficult to quantify such benefits with precision, estimates are available. An analysis conducted by the WEFA Group predicts that long-distance rates will drop by 25 percent as a result of Bell company in-region, interLATA entry. WEFA Study at p. 11; Raimondi Aff. at p. 38 (App. C at Tab 62). The study estimates an additional 13,000 new jobs will be created in South Carolina as a result and that the total benefit of new long distance competition for South Carolinians will rise to $1.2 billion after five years. WEFA Study at pp. 1-2, 21. Independent economists have confirmed that the WEFA model was based on reliable assumptions and would produce reliable results in South Carolina. Hefner Aff. ¶ 88 (App. C at Tab 62). The SCPSC in fact noted that these studies were "unrefuted" by BellSouth's opponents. Compliance Order at 62.

The estimates presented to the SCPSC are consistent with the work of other prominent economists. Dr. Paul MacAvoy of Yale projects that, nationwide, the total gains to consumers from unrestricted Bell company entry into the long-distance market would be as high as $306 billion, even if AT&T, MCI, and Sprint "maintain their tacitly collusive pricing strategies." MacAvoy Study at p. 185. During debates on the 1996 Act, Congress relied upon estimated savings of $333 billion from greater long distance competition. 141 Cong. Rec. S704 (Feb. 1, 1996) (statement of Sen. Ford). Relying upon actual market experience with local telephone company entry into long distance as well as incumbent LECs' economic incentive to lower prices upon vertical integration,[51] Professor Hausman anticipates that prices would fall by about 17-18 percent as a result of in-region entry by the Bell companies, and that residential customers alone stand to benefit by about $7 billion per year. Hausman Aff. ¶¶ 5, 20-23.

Aware of these potential benefits, South Carolinians have rallied around BellSouth's application. Attached as Tabs 1A-1H of Appendix D are more than 450 letters supporting BellSouth's entry into long distance in the South Carolina. These letters come from people in every walk of life: the Governor and Attorney General of South Carolina and other State and local officials, community and educational organizations, businesses, community leaders, and everyday consumers. This Commission should give the views of these hundreds of supporters — representing the interests of thousands and thousands more in the State — at least as much weight in ascertaining the public interest as the self-serving protestations of BellSouth's competitors.

[51] Professor Hausman explains that where a single entity earns margins on both access services and retail long distance, it has an incentive to lower price to expand its market share. Hausman Aff. ¶¶ 10-12.

D. BellSouth's Entry into the InterLATA Market, Subject to Extensive Statutory and Regulatory Safeguards, Presents No Risk to Competition

For all its potential strengths as a competitor, BellSouth has absolutely no ability to impede competition by entering the interLATA market. The 1996 Act and regulatory reforms have rendered 20-year-old worries about cross-subsidy and network discrimination obsolete.

1. Regulation and Practical Constraints Make "Leveraging" Strategies Impossible to Accomplish

In light of the federal and state safeguards that prevent Bell companies from engaging in anticompetitive conduct upon entering long distance, the Commission recently held that the Bell companies should be regulated as non-dominant when they provide in-region, interLATA services.[52] It found that Bell companies could not drive other interexchange carriers from the market through cost misallocation, that federal and state price caps reduce incentives to misallocate costs, and that existing safeguards "will constrain a BOC's ability to allocate costs improperly and make it easier to detect any improper allocation of costs that may occur." Id. ¶ 105. The Commission likewise dismissed fears of predation against the established long distance incumbents, id. ¶ 108; found that the numerous protections against discrimination will prevent Bell companies from gaining market power upon entry through such tactics, id. ¶¶ 111-119; and concluded that any risk of price squeezes can be addressed through FCC procedures and the antitrust laws, id. ¶¶ 128-129. Finally, the Commission recognized "that the entry of the

[52] Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace, FCC 97-142 (rel. Apr. 18, 1997) ("BOC Non-Dominance Order").

BOC interLATA affiliates into the provision of in-region, interLATA services has the potential to increase price competition and lead to innovative new services and market efficiencies." Id. ¶ 134.

Each of these conclusions is buttressed by the success that federal and state regulators have had in regulating Bell companies over the years, as well as by the new, additional safeguards imposed by the 1996 Act and the Commission's implementing regulations. As a former Deputy Assistant Attorney General for Economics in the current Administration's Antitrust Division explains, existing safeguards "expressly and comprehensively" address potential harms. Gilbert Aff. ¶ 43.

a. Cost Misallocation. Theories that BellSouth might shift costs incurred in providing interLATA services to local ratepayers, thereby giving itself a competitive edge as an interLATA carrier, depend upon the assumption that BellSouth "is regulated under rate-of-return regulation." Notice of Proposed Rulemaking, Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended, 11 FCC Rcd 18877, 18882-83, ¶ 7 (1996) ("Non-Accounting Safeguards NPRM.")[53]

To cure this problem, the Commission has totally overhauled its approach to rate regulation, see Hausman Aff. ¶ 34, as has the SCPSC, see Woroch Aff. ¶¶ 53, 67. The Commission adopted a price cap regime that sets maximum rates almost entirely without regard

[53] The Department of Justice contended in supporting approval of the MFJ that the Bell System's alleged practice of subsidizing its competitive offerings at ratepayers' expense "stem[med] . . . directly from AT&T's status as a rate-of-return regulated firm . . . ." Competitive Impact Statement at 13, United States v. AT&T, No. 74-1698 (D.D.C. Feb. 10, 1982).

to costs, thereby giving LECs "a powerful profit incentive" to cut the costs of their regulated services. National Rural Telecom Ass'n v. FCC, 988 F.2d 174, 178 (D.C. Cir. 1993). There is no "reward for shifting costs from unregulated activities into regulated ones, for the higher costs will not produce higher legal ceiling prices." Id.; see Non-Accounting Safeguards NPRM, 11 FCC Rcd at 18942-43, ¶ 136 (Commission's price cap policies "reduc[e] the potential that the BOCs would improperly allocate the costs of their affiliates' interLATA services"); Hausman ¶ 34. Indeed, the Commission has described price caps regulation as providing strong "efficiency incentives" to keep down costs allocated to regulated services. Report and Order, Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996, 11 FCC Rcd 17539, 17605-06, ¶ 145 ("Accounting Safeguards Order"); see also Illinois Public Telecommunications Ass'n v. FCC, 117 F.3d 555, 570 (D.C. Cir. July 1, 1997) (under price caps "risk of loss" is borne by "investors rather than ratepayers"), clarified, Case No. 96-1394, slip op. (D.C. Cir. Sept. 16, 1997); Hausman Aff. ¶¶ 35-36.[54]

Congress nevertheless took steps to address supposed worries about possible cost misallocation. In section 272 of the 1996 Act, Congress sharply reduced opportunities for cost-shifting by requiring that a Bell company provide long distance through an affiliate that has

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[54] To the extent that sharing may formerly have been a concern, see Non-Accounting Safeguards NPRM, 11 FCC Rcd at 18942-43, ¶ 136, that concern is addressed by the Commission's recent decision to eliminate sharing entirely. Fourth Report and Order in CC Docket No. 94-1 and Second Report and Order in CC Docket No. 96-262, Price Cap Performance Review for Local Exchange Carriers and Access Reform Charge, FCC 97-159, ¶¶ 147-155 (rel. May 21, 1997); see Hausman ¶ 34.

separate facilities, employees, and record-keeping from the local telephone company. 47 U.S.C. § 272. Moreover, Congress reinforced structural separation with demanding accounting requirements. See id. § 272(d), Hausman Aff. ¶ 37. Legislators concluded, after hearing arguments on all sides, that these statutory safeguards and the Commission's implementing rules would be sufficient to deal with concerns about Bell company cost misallocation. See, e.g., 47 U.S.C. § 254(k) (requiring Commission to implement regulations as necessary "to ensure that" revenues from regulated services are not used to subsidize competitively provided services). The Commission has likewise expressed confidence in the efficacy of structural separation in various contexts.[55]

The Commission's post-Act rulemakings to implement section 272's safeguards, together with its pre-existing regulations, guarantee that the statutory protections will amply suffice to protect against cost-misallocation. Indeed, the Commission has explained that its preexisting "cost allocation and affiliate transactions rules, in combination with audits, tariff review, and the complaint process, have proven successful at protecting regulated ratepayers from bearing the risks and costs of incumbent local exchange carriers' competitive ventures." Accounting Safeguards Order, 11 FCC Rcd at 17550-51, ¶ 25. It reasoned that these rules together "will effectively prevent predatory behavior that might result from cross-subsidization," and that

[55] Report and Order, Inquiry into the Use of the Bands 825-845 MHZ and 870-890 for Cellular Communications Sys., 86 FCC 2d 469, 494, ¶ 50 (1981) (cellular); Amendment of Section 64.702 of the Commn's Rules and Regulations (Second Computer Inquiry); Final Decision, Amendment of Section 64.702 of the Commission's Rules and Regulations (Second Computer Inquiry), 77 F.C.C.2d 384, 453 ¶ 177 (Bell System), aff'd sub nom. Computer and Communications Indus. Ass'n v. FCC, 693 F.2d 198, 211 (D.C. Cir. 1982).

because they "have proven generally effective" there was "no reason to require a change to a different system." Id. ¶¶ 28, 108.

South Carolina regulators have implemented a parallel regulatory regime that contains many of these same protections. In endorsing BellSouth's application for interLATA entry, the SCPSC rejected interexchange carriers' predictions of anticompetitive conduct, explaining that "just as [BellSouth's] provision of long distance services will not diminish its obligations under the checklist, it also will not diminish its obligations under Sections 251 and 252 of the Act, South Carolina law, FCC and [SCPSC] regulations and its binding agreements." Compliance Order at 65. Like the Commission, the SCPSC has abandoned rate-of-return regulation in favor of price-cap regulation.[56] The SCPSC also adheres to this Commission's accounting requirements, imposing similar record-keeping and reporting requirements and carrying out periodic audits. Woroch Aff. ¶¶ 53, 67; Compliance Order at 65. Moreover, the South Carolina Attorney General has committed his office's resources "to pursue fully any allegation of anti-competitive acts " in connection with BellSouth's interLATA entry. Letter from Charles Molony Condon, South Carolina Attorney General, to Federal Communications Commission at 2 (Sept. 5, 1997) (App. D at Tab 1A).

b. Other Pricing Strategies. Just as cost misallocation would be impossible to accomplish, BellSouth would not and could not raise the cost of its access services in an effort to

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[56] See Order Granting Alternative Regulation and Approving Plan as Modified, Application of BellSouth for Alternative Regulation (Price Protection Plan), No. 96-19, Docket No. 95-720-C, 1 (SCPSC Jan. 30, 1996) (approving plan "to cap the rates for certain categories of services, including basic exchange services").

effectuate a "price squeeze" on other interexchange carriers.[57] The Commission has cited a host of factors that "constrain the ability of a [Bell company or its] interLATA affiliate to engage in a predatory price squeeze," and concluded that Bell companies "will not be able to engage in a price squeeze to such an extent that the [Bell company] interLATA affiliates will have the ability, upon entry or soon thereafter, to raise price by restricting their own output." BOC Non-Dominance Order ¶ 129. The Commission likewise concluded that a strategy of providing long distance services below cost to drive out competitors could not be profitable for Bell companies because losses incurred in predation could not later be recovered through supra-competitive pricing. Id. ¶ 108; see also Non-Accounting Safeguards NPRM, 11 FCC Rcd at 18943, ¶ 137; Hausman Aff. ¶ 38.

Wholly aside from regulatory safeguards, "predatory pricing schemes are rarely tried, and even more rarely successful."[58] See Roberts Aff. ¶ 54 (App. A at Tab 10). In an industry with standardized technologies and sophisticated incumbents, it is "especially unlikely" that BellSouth could employ the classic predatory strategy of lowering prices below cost to affect competitors' assessments of future competition. Id. ¶¶ 24, 46-48; see also Gilbert Aff. ¶¶ 43-46. Realistically, moreover, any attempt to drive out large and well-financed incumbent carriers who have made mammoth sunk investments would be doomed. Roberts Aff. ¶¶ 46-47.

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57. See generally Town of Concord v. Boston Edison Co., 915 F.2d 17, 18 (1st Cir. 1990) (per Breyer, J.) (discussing theory of price squeezes), cert. denied, 499 U.S. 931 (1991).

58. Brooke Group v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 226 (1993) (citations omitted); see id.

c. Price Discrimination. Perhaps the weakest of all theories advanced by those with a vested interest in delaying interLATA competition is that Bell companies might discriminate in the pricing of their exchange access services. The Commission has for years "require[d] any exchange carrier offering interexchange service to impute to itself the same costs that it uses to develop the access rates that it charges its interexchange customers." Order on Reconsideration, Policy and Rules Concerning Rates for Dominant Carriers, 6 FCC Rcd 2637, 2714 (1991). Consistent with that regulatory requirement, Congress specifically provided that the Bell company must charge its affiliate, or impute to itself, "an amount for access to its telephone exchange service and exchange access that is no less than the amount charged to any unaffiliated interexchange carriers for such service." 47 U.S.C. § 272(e)(3). The Commission thus rightly has concluded that "the statutory and regulatory safeguards . . . will prevent a [Bell company] from discriminating to such an extent that its interLATA affiliate would have the ability, upon entry or shortly thereafter, to raise the price of in-region, interstate, domestic, interLATA services." BOC Non-Dominance Order ¶ 119.

d. Technical Discrimination. Theories that BellSouth might impede competition by engaging in technical discrimination are equally unfounded. AT&T, British Telecom/MCI, and Sprint/Centel/Deutsche Telekom/France Telecom are sophisticated, vertically integrated goliaths with revenues much greater than BellSouth's and the expertise and resources to detect and challenge systematic discrimination. See Gilbert Aff. ¶¶ 46-47, 49. Indeed, to state how discrimination against them would have to occur is virtually to prove its impossibility: In order to gain an anticompetitive edge, BellSouth would have to provide inferior access services to its major competitors, without disrupting its own local or long distance services, in a fashion that is invisible to other interexchange carriers and regulators, yet so apparent to customers that it drives them to switch to BellSouth's long distance service, but not the service of some other competitor. See Hausman Aff. ¶ 40; see also Gilbert Aff. ¶¶ 46-47 (no harm to competition unless discrimination raises consumer prices). When one considers these realities, it is not surprising that incumbent interexchange carriers never have produced specifics (much less hard evidence) as to the precise form hypothetical future discrimination would take, how it is feasible, what effect it would have on consumer decision-making, what costs it would impose on interexchange carriers, or how it would reduce competition and increase prices.

To accomplish discrimination, BellSouth would have to circumvent the mechanization of its technical and operations systems, including assignment and provisioning processes. It would have to bypass the SONET capabilities used by many interexchange carriers to reconfigure immediately their networks should a malfunction or service degradation occur. Gunter Aff. ¶¶ 40-42. If technically possible at all, this would require substantial and visible investments, participation by large numbers of employees, and the cooperation of hardware and software vendors who have no interest in favoring BellSouth's interLATA services operations, all of which make such a strategy unthinkable. Id. ¶ 40. Of course, there also would be no guarantee that customers who are unhappy with their existing long distance carrier would switch to BellSouth; targeted discrimination against, say, Sprint, would send many customers to AT&T and MCI, giving BellSouth no benefit. Cf. United States v. Western Elec. Co., 993 F.2d 1572,